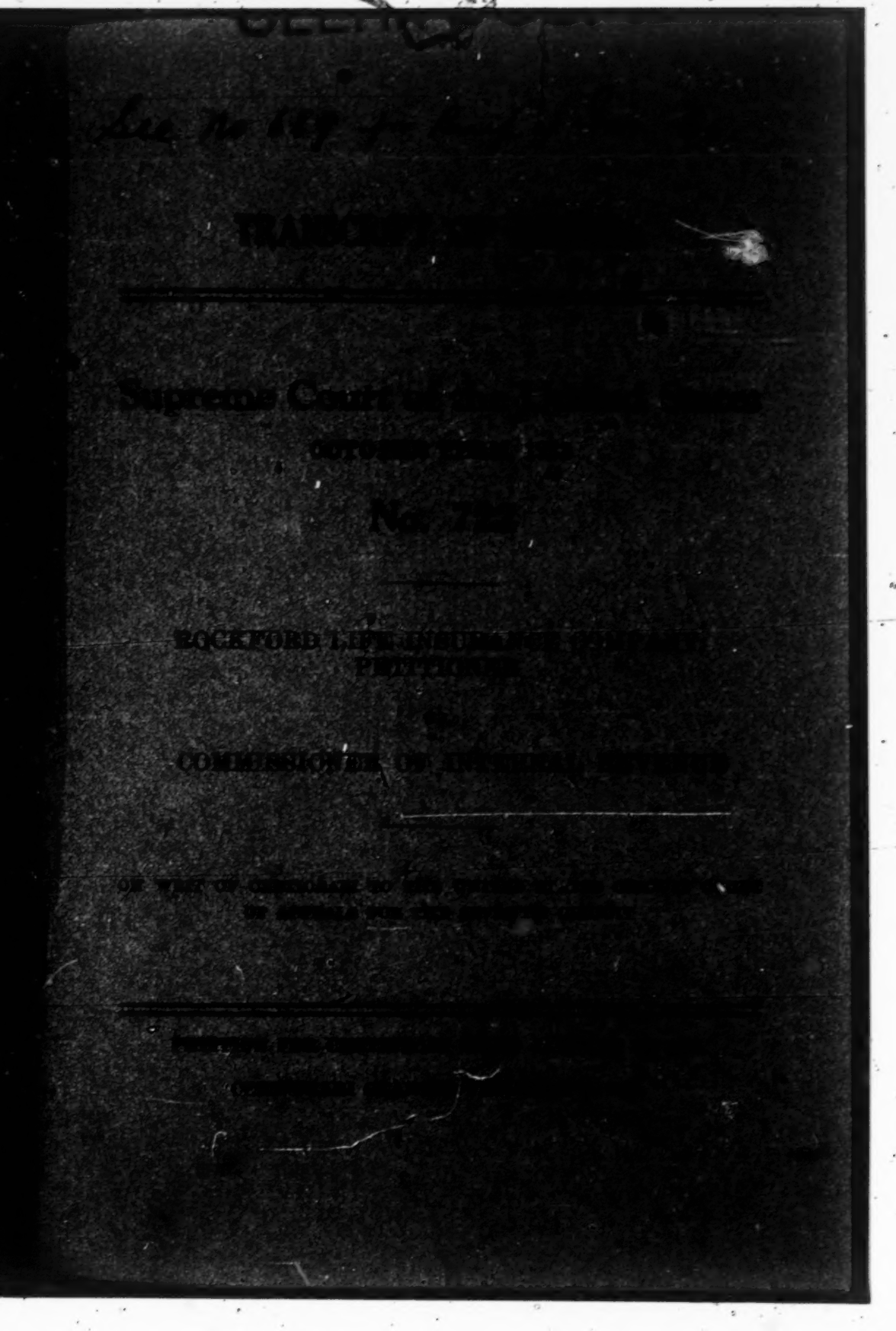

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933

No. 722

ROCKFORD LIFE INSURANCE COMPANY,
PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 60915

ROCKFORD LIFE INSURANCE CO., Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appearances:

For Petitioner: B. W. Flinn, C. P. A., M. L. Seidman, C. P. A.

For Respondent: Thos. F. Callahan, Esq.

DOCKET ENTRIES

1931.

Dec. 18. Petition received and filed. Taxpayer notified. (Fee paid.)

Dec. 18. Copy of petition served on General Counsel.

1932.

Feb. 5. Answer filed by General Counsel.

Feb. 12. Copy of answer served on taxpayer—assigned to General Calendar.

July 11. Hearing set Sept. 28, 1932.

Sept. 7. Notice of appearance of M. L. Seidman as counsel filed.

Sept. 17. Motion for leave to amend petition, amendment tendered, filed by taxpayer.

Sept. 28. Hearing had before C. R. Arundell—submitted on merits. Stipulation of facts filed.

Oct. 7. Agreement to correct stipulation of facts filed.

Oct. 11. Transcript of hearing Sept. 28, 1932 filed.

Oct. 12. Motion for leave to amend granted.

Oct. 21. Brief filed by taxpayer.

Nov. 9. Memorandum opinion rendered—C. R. Arundell, Division 7. Decision will be entered under Rule 50.

Dec. 17. Answer to amendments to petition filed by General Counsel. 12/22/32 copy served.

Dec. 29. Notice of settlement filed by taxpayer. 1/4/33 copy served.

1933.

Jan. 4. Hearing set Jan. 25, 1933 on settlement.

Jan. 7. Notice of settlement filed by General Counsel. 1/12/33 copy served.

[fol. 2]

Jan. 14. Consent to settlement filed by taxpayer.

Jan. 24. Decision entered—C. R. Arundell, Division 7.

Apr. 6. Petition for review by U. S. Circuit Court of Appeals, 7th Circuit, with assignments of error filed by General Counsel.

Apr. 14. Proof of service filed by General Counsel (taxpayer).

Apr. 19. Proof of service filed by General Counsel (attorney).

May 25. Præcipe with proof of service thereon filed.

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 60915

ROCKFORD LIFE INSURANCE COMPANY, 327 East State Street, Rockford, Illinois, Petitioner,

versus

COMMISSIONER OF INTERNAL REVENUE, Washington, D. C., Respondent

PETITION—Filed Dec. 18, 1931

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Symbols IT:AR:D-6 LF-60D) dated October 20, 1931 and as a basis of its proceedings alleges as follows:

1. The Petitioner is an Illinois corporation with its principal office at Rockford, Illinois.

2. The notice of deficiency, a copy of which is attached and marked Exhibit "A", was mailed to the petitioner on October 20, 1931.

3. Taxes in controversy are the income taxes for the calendar year 1929 and are for $443.63.

4. The determination of tax set forth in said notice of deficiency is based upon the following errors.

(a) The Commissioner of Internal Revenue in computing the tax liability for the calendar year 1929 has erroneously [fol. 3] refused to allow as a deduction depreciation sustained on the home office building of $1,813.71.

(b) The Commissioner of Internal Revenue, in computing the tax liability for the calendar year 1929, has erroneously refused to allow as a deduction taxes paid on the home office building of $1,808.03.

(c) The Commissioner of Internal Revenue, in computing the tax liability for the calendar year 1929, has erroneously refused to allow as a deduction an expenditure for repairs to the home office building of $411.31.

5. The facts upon which the petitioner relies as a basis for its proceedings are as follows:

(a) In 1926 the petitioner acquired by purchase at a cost of $75,000.00 a home office building. Of the purchase price of $75,000.00, $41,250.00 was the value of the land and $33,750.00 the value of the building. In 1926 the petitioner expended $2,524.21 for remodeling the home office building. The total cost of the building, subject to depreciation, is $33,750.00 representing original cost plus cost of remodeling of $2,524.21, making a total cost subject to depreciation of $36,274.21. The estimated life of the home office building when acquired in 1926 was twenty years. The annual depreciation is five per cent. Upon the examination of petitioner's federal income tax return for the calendar year 1929, the respondent refused to allow the deduction for depreciation sustained on the home office building of $1,813.71.

(b) During 1929 the tax assessor of Rockford Township, Rockford, Illinois, made an assessment against the petitioner for real estate taxes on its home office building of $1,808.03, which were duly paid, and claimed as a deduction from taxable income on the original corporation income tax return filed for 1929. Upon the examination of petitioner's federal income return for the year 1929, the respondent refused to allow the deduction of real estate taxes

paid on the home office building of $1,808.03 and increased petitioner's net income by that amount.

(c) During 1929 the petitioner expended for repairs to the home office building $411.31, which did not prolong the life of the building. The building repairs of $411.31 were claimed as a deduction on the original corporation income tax return filed for 1929. Upon the examination of petitioner's income tax return for the calendar year 1929 the respondent refused to allow the expenditure for repairs to the home office building of $411.31 and increased petition-
[fol. 4] er's net income by that amount.

6. The petitioner prays for relief from the deficiency asserted by the respondent on the following and each of the following particulars:

(a) That in arriving at the tax liability of the petitioner for the calendar year 1929 the depreciation sustained on the home office building of $1,813.71 should be allowed as a deduction from taxable income.

(b) That in arriving at the tax liability of the petitioner for the calendar year 1929 the real estate taxes paid on the home office building of $1,808.03 should be allowed as a deduction from taxable income.

(c) That in arriving at the tax liability for the petitioner for the calendar year 1929 the expenditure for repairs to the home office building of $411.31 should be allowed as a deduction from taxable income.

Whereas the petitioner prays that this Board may hear and re-determine the deficiency herein alleged.

B. W. Flinn, C. P. A. B. W. Flinn, Accountant for Taxpayer, 502 Manufacturers National Bank Bldg., Rockford, Illinois.

Duly sworn to by Roy Hanson. Jurat omitted in printing.

[fol. 5] EXHIBIT "A" TO PETITION

Treasury Department, Washington

Office of Commissioner of Internal Revenue

Address reply to Commissioner of Internal Revenue and refer to Rockford Life Insurance Company, 327 East State Street, Rockford, Illinois.

Oct. 20, 1931.

SIRS: You are advised that the determination of your tax liability for the year 1929 discloses a deficiency of $607.53, as shown in the statement attached.

In accordance with section 272 of the Revenue Act of 1928, notice is hereby given of the deficiency mentioned. Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter, you may petition the United States Board of Tax Appeals for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the enclosed agreement form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this agreement will expedite the closing of your return by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the enclosed agreement, or on the date assessment is made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiency.

Respectfully, David Burnet, Commissioner (Signed),
by J. C. Wilmer, Deputy Commissioner.

Enclosures: Statement. Form 882. Form 870. Schedules 1 to 2, inclusive. Exhibit A.

[fol. 6] Statement

IT:AR:D-6.
LF-60D.

In re: Rockford Life Insurance Company, 327 East State Street, Rockford, Illinois

Tax Liability

Year	Tax liability	Tax assessed	Deficiency
1929	$3,639.69	$3,032.16	$607.53

The change in tax from that shown by the revenue agent's report is due to adjustments made by this office as explained herein. These adjustments were also explained in Bureau letter dated July 29, 1931.

With reference to fees for drawing papers on mortgage loans, the Bureau holds that such receipts do not come

within the meaning of the provisions of section 202(a) of the Revenue Act of 1928 and should, therefore, be excluded from gross income.

Rockford Life Insurance Company, Year Ended December 31, 1929

Schedule 1

Net Income

Net income as disclosed by return		$27,565.11
As corrected		33,088.08
Net adjustment		$5,522.97
Unallowable deductions and additional income:		
(a) Investment expenses	$1,195.27	
(b) Depreciation	3,261.42	
(c) Taxes	655.37	
(d) Other expenses of home office building	411.31	
Total		5,523.37
Nontaxable income and additional deductions:		
(e) Error in computation of 4 per cent of the mean of the reserve funds		:40
Net adjustment as above		$5,522.97

[fol. 7]

Schedule 1-A

Explanation of Items Changed

(a) The following investment expenses have been allowed in lieu of one-fo-rth of one per cent of the mean of the invested assets. This action is in accordance with section 203(a)(5) of the Revenue Act of 1928.

Allocation of salaries of officers and employees to the investment department:

Officers and employees	Salary	Time devoted to department	Amount allocated
President	$7,750.00	10%	$775.00
Secretary	4,560.00	20%	912.00
Counsel	1,800.00	50%	900.00
Employee	1,800.00	100%	1,800.00
Total			$4,387.00

One-fourth of one per cent of the mean of the invested assets	5,582.27
Amount disallowed	$1,195.27

Explanation of Items Changed

(b) The Bureau holds that depreciation may only be taken on that portion of the cost of furniture and fixtures used in the investment department. In the absence of any specific allocation of such cost to the investment department, allocation has been made upon the basis of the ratio of investment income to total income computed as follows:

Income from interest and rents	$123,248.44
Income from premiums	627,899.33
Total	$751,147.77
$123,248.44 ÷ $751,147.77 × $1,783.02 (depreciation as shown in exhibit A)	292.56
Depreciation deducted on return	3,553.98
Depreciation disallowed	$3,261.42

In this connection, you are advised that the Commissioner of Internal Revenue has not acquiesced in the decision of [fol. 8] the United States Board of Tax Appeals in the case of the Independent Life Insurance Company of America published in volume 17 B. T. A., page 757. Inasmuch as the rental value of the space occupied in the home office building was not included in gross income, depreciation on such building has been disallowed. This action is held to be in accordance with section 203(b) of the Revenue Act of 1928.

(c) This amount represents the difference between the taxes on the home office building, $1,808.03, deducted on the

return but disallowed as explained in paragraph three, item (b), and $1,152.66, taxes paid for shareholders and not deducted on return, but allowable under section 203(a)(6) of the Revenue Act of 1928.

(d) Repairs to home office building have also been disallowed as explained in paragraph three, item (b).

(e) This adjustment is made to correct an error on your return as shown in the following computation:

Reserve funds at the beginning of the year	$1,983,136.93
Corrected reserve funds at the end of the year	2,232,520.00
Total	$4,215,656.93
Mean of the reserve funds	2,107,828.47
Four per cent of the mean of the reserve funds	84,313.14
Amount claimed on return	84,312.74
Additional amount allowed	.40

Schedule 2

Computation of Tax

Net income for taxable year	$33,088.08
Income tax at 11%	3,639.69
Total previously assessed	3,032.16
Additional tax to be assessed	$607.53

[fol. 9]

EXHIBIT A

IT:AR:D-6. LF.

Rockford Life Insurance Company, Rockford, Illinois.

Furniture and Fixtures

Depreciation Schedule

Year and month		Corrected balance close of period	Additions or (reductions)	Rate	Total to December 31, 1926	1927	1928	1929
1916	Balance	$2,778.66		(A) 10%	$2,778.66	.....	.....	.....
1917	July 1	3,223.17	444.51	(B)	422.27	22.24	.....	.....
1918	July 1	3,449.71	226.54	(C)	192.52	22.65	$11.37	.....
1919	July 1	2,745.91	(703.80)	(D)	(527.85)	(70.38)	(70.38)	($35.19)
1920	July 1	3,018.46	272.55		177.17	27.26	27.26	27.26
1921	July 1	3,695.32	676.86		372.28	67.69	67.69	67.69
1922	July 1	5,084.05	1,388.73		624.92	138.87	138.87	138.87
1923	July 1	6,437.39	1,353.34		437.66	135.33	135.33	135.33
1924	July 1	9,378.92	2,941.53		735.38	294.15	294.15	294.15
1925	July 1	10,507.13	1,128.21		169.23	112.82	112.82	112.82
1926	July 1		5,405.93		270.30	540.59	540.59	540.59
1926		13,134.40	(2,778.66)	(A) 100% Dep.	.....	.....	.....	.....
1927	July 1		2,949.29		.....	147.47	294.93	294.93
1927		15,639.18	(444.51)	(B) 100% Dep.	.....	.....	.....	.....
1928	July 1		1,408.44		.....	.....	70.42	140.84
1928		16,821.08	(226.54)	(C) 100% Dep.	.....	.....	.....	.....
1929	July 1		1,314.50		.....	.....	.....	65.73
1929		18,839.38	703.80	(D) 100% Dep.	.....	.....	.....	.....
Total Depreciation					$5,688.54	$1,438.69	$1,623.15	$1,783.02

[fol. 10] BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

ANSWER—Filed Feb. 5, 1932

Now comes the Commissioner of Internal Revenue, the respondent herein, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, and for answer to the petition heretofore filed in this appeal, admits and denies as follows:

1 and 2. Admits the allegations contained in paragraphs 1 and 2 of the petition.

3. Admits that the taxes in controversy are the income taxes for the calendar year 1929. Denies the remaining allegations contained in paragraph 3 of the petition.

4 (a) (b) and (c). Denies that the respondent committed the errors alleged in subparagraphs (a) (b) and (c) of paragraph 4 of the petition.

5 (a). Admits that the respondent has not allowed as a deduction for the calendar year 1929 alleged depreciation on the home office building in the amount of $1,815.71. Denies the remaining allegations contained in subparagraph (a) of paragraph 5 of the petition.

5 (b). Admits that the respondent has not allowed as a deduction from gross income for the year 1929 the amount of $1,808.03, alleged taxes paid on the home office building. Denies the remaining allegations contained in subparagraph (b) of paragraph 5 of the petition.

5 (c). Admits that the respondent has not allowed as a deduction from gross income for 1929 the amount of $411.31, alleged expenditure for repairs to the home office building. Denies the remaining allegations contained in subparagraph (c) of paragraph 5 of the petition.

Denies generally and specifically each and every allega-
[fol. 11] tion contained in the petition not hereinbefore expressly admitted, qualified or denied.

Wherefore, it is prayed that the Board redetermine the amount of the deficiency involved in this proceeding to be equal to the amount determined by the Commissioner, plus

any additional amount which may arise from the correction of any error or errors that may have been committed by the Commissioner. Claim is hereby asserted for the increased deficiency, if any, resulting from such redetermination.

(Signed) C. M. Charest, General Counsel, Bureau of Internal Revenue. Of Counsel: L. W. Creason, Special Attorney, Bureau of Internal Revenue.

BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

AMENDMENTS TO PETITION—Filed Sept. 27, 1932

Now comes the petitioner, by its counsel, M. L. Seidman, and moves that the petition in this cause be amended in the following respects:

1. That paragraph "4" be amended to include sub-paragraph "(d)", reading as follows:

"(d) The Commissioner of Internal Revenue erroneously failed to allow the full amount of depreciation which petitioner sustained in 1929 in connection with its furniture and fixtures, allowing only the sum of $292.56 applicable to petitioner's investment income, and denying as a deduction the sum of $1,490.46 applicable to petitioner's life insurance business."

2. That paragraph "5" be amended to include sub-paragraph "(d)", reading as follows:

[fol. 12] "(d) Petitioner's furniture and fixtures employed in its business in 1929 were acquired at a cost of $18,839.38, as determined by the Commissioner of Internal Revenue in Exhibit "A" attached to the deficiency notice; and a reasonable allowance for depreciation on said furniture and fixtures for the year 1929 was $1,783.02, as determined by the Commissioner of Internal Revenue in the deficiency notice. The Commissioner of Internal Revenue allowed as a deduction in computing petitioner's 1929 net income only $292.56 of said depreciation, erroneously disallowing the balance of $1,490.46 on the ground that peti-

tioner was not entitled to deduct depreciation on furniture and fixtures applicable to its life insurance business."

3. That paragraph "6" be amended to include sub-paragraph "(d)", reading as follows:

"(d) In arriving at petitioner's net income and tax liability for the calendar year 1929, the deduction for depreciation on furniture and fixtures be increased from $292.56 to $1,783.02."

Dated September 16, 1932.

M. L. Seidman, M. L. Seidman, C. P. A., Counsel for Petitioner (Post Office Address:) 2 Lafayette Street, New York City.

Duly sworn to by Roy Hanson. Jurat omitted in printing.

[fol. 13] BEFORE U. S. BOARD OF TAX APPEALS

ANSWER TO AMENDMENTS TO PETITION—Filed Dec. 17, 1932

Now comes the Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, and for answer to the amendments to the petition filed herein, denies as follows:

1. Denies each and every allegation contained in paragraph 1 of the Amendments to Petition.

2. Denies each and every allegation contained in paragraph 2 of the Amendments to Petition.

3. Denies each and every allegation contained in paragraph 3 of the Amendments to Petition.

Wherefore, it is prayed that the appeal be denied and the tax as shown in the deficiency notice be in all respects approved.

(Signed) C. M. Charest, General Counsel, Bureau of Internal Revenue. Of counsel: Thos. F. Callahan, Special Attorney, Bureau of Internal Revenue.

BEFORE U. S. BOARD OF TAX APPEALS

STIPULATION OF FACTS—Filed at Hearing Sep. 28, 1932. Admitted in Evidence Sep. 28, 1932

It is hereby stipulated and agreed by and between the parties to the above-entitled appeal, by their respective counsel, that the Board may find the following facts:

1. That the petitioner, Rockford Life Insurance Company, is a life insurance company incorporated under the laws of the State of Illinois, with its principal office located at Rockford, Illinois.

[fol. 14] 2. That throughout the year 1929 petitioner owned the land and building located at 327 East State Street, Rockford, Illinois, which it acquired in 1926 at a total cost of $77,524.21, made up as follows:

Land	$41,250.00
Building	33,750.00
Permanent improvements to building	2,524.21
Total	$77,524.21

A reasonable allowance for exhaustion, wear and tear of this building, and the improvements thereto, sustained by the petitioner during the year 1929, is $1,813.71.

3. That the book value as of December 31, 1929, of the land and building located at 327 East State Street, Rockford, Illinois, which the petitioner owns, was $71,176.23.

4. In 1929, petitioner paid annual real estate taxes covering premises 327 East State Street, Rockford, Illinois, to the tax assessor of Rockford Township, Rockford, Illinois, for the year 1929, in the sum of $1,808.03.

5. In 1929, petitioner incurred and paid expenses for ordinary and necessary repairs to the premises 327 East State Street, Rockford, Illinois, in the sum of $411.31.

6. The entire building was occupied by the petitioner, which included no rent income from the premises on its 1929 Federal income tax return other than the sum of $15.00.

7. The petitioner, in its income tax return for 1929, did not include in its gross income the rental value of any real estate owned and occupied by it in whole or in part.

8. Respondent determined that a reasonable allowance for depreciation of petitioner's furniture and fixtures for the year 1929 was $1,783.02 (see Exhibit "A" attached to deficiency notice, which in turn is Exhibit "A" attached to the petition) but allowed only $292.56 of this amount in computing petitioner's net income for 1929, holding that the balance of depreciation on furniture and fixtures applied to petitioner's insurance business and was therefore not deductible.

9. The respondent, in computing the net income upon which the deficiency notice of October 20, 1931, is based, has not allowed any deduction on account of depreciation, taxes, and repairs referred to in items 2, 3 and 4 above.

It is further stipulated and agreed that the case shall [fol. 15] stand submitted and counsel for the parties shall have thirty days for the submission of briefs.

M. L. Seidman, Counsel for Petitioner. C. M. Charest, General Counsel, Bureau of Internal Revenue, Counsel for Respondent.

BEFORE U. S. BOARD OF TAX APPEALS

AGREEMENT AS TO STIPULATION OF FACTS—Filed Oct. 7, 1932

The parties to this proceeding hereby agree that paragraph 9 of the Stipulation of Facts filed with the Board on September 28, 1932, reading as follows:

The respondent, in computing the net income upon which the deficiency notice of October 20, 1931, is based, has not allowed any deduction on account of depreciation, taxes, and repairs referred to in items 2, 3, and 4 above.

shall be stricken, and in lieu thereof the following paragraph shall be substituted:

The respondent, in computing the net income upon which the deficiency notice of October 20, 1931, is based, has not

allowed any deduction on account of depreciation, taxes, and repairs referred to in items 2, 4, and 5 above.

(Signed) M. L. Seidman, Counsel for Petitioner.
C. M. Charest, General Counsel, Bureau of Internal Revenue, Counsel for Respondent.

vgk 9/28/32.

[fol. 16] BEFORE U. S. BOARD OF TAX APPEALS

M. L. Seidman, C. P. A., for petitioner.
Thomas F. Callahan, Esq., for the respondent.

MEMORANDUM OPINION—Filed Nov. 9, 1932

ARUNDELL:

The petitioner is an Illinois corporation engaged in the life insurance business. In its income tax return for 1929 the petitioner did not include in gross income any sum for rental value of the building owned and occupied by it, but claimed as deductions certain sums for depreciation, taxes and repairs on account of the property and depreciation on furniture and fixtures. The respondent disallowed the former because the rental value of the space occupied in the building was not included in gross income and allowed only $292.56 of the amount deducted for depreciation on furniture and fixtures, holding that the remainder applied to petitioner's insurance business, and was, therefore, not deductible. The respondent determined a deficiency of $607.53 in income tax partly as the result of these adjustments. Whether his action was proper is the only question presented for decision.

The several amounts deductible from gross income, in case we hold in favor of the petitioner, are embodied in a stipulation of facts, which we adopt as our findings of fact.

Counsel for the respondent concedes that the cases of Independent Life Insurance Co., 17 B. T. A. 757 and Lafayette Life Insurance Co., 26 B. T. A. —, are contrary to his manner of treating the items. Those cases, as well as Reserve Loan Life Insurance Co., 18 B. T. A. 359 and Two-Republics Life Insurance Co., 21 B. T. A. 1355, in which like conclusions were reached, control the decision here. Accordingly, we hold that the several amounts set forth in

the stipulation of facts representing reasonable depreciation on the building and furniture and fixtures, and taxes paid on and repairs made to the building, are deductible from gross income.

Decision will be entered under Rule 50.

Entered Nov. 9, 1932.

[fol. 17] BEFORE U. S. BOARD OF TAX APPEALS

DECISION

Pursuant to memorandum opinion entered November 9, 1932, the respondent herein, on January 7, 1933 having filed a proposed redetermination for the year 1929, and the petitioner on January 14, 1933, having filed notice of acquiescence to the said proposed redetermination, it is

Ordered and Decided that there is an overpayment for the year 1929 in the amount of $750.05.

Enter: Entered Jan. 24, 1933.

(Signed) C. Rogers Arundell, Member. (Seal.)

vlh.

BEFORE U. S. BOARD OF TAX APPEALS

NOTICE OF FILING PETITION FOR REVIEW—Filed April 14, 1933

To Rockford Life Insurance Company, 327 East State Street, Rockford, Illinois:

You are hereby notified that the Commissioner of Internal Revenue did, on the 6th day of April, 1933, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Seventh Circuit, of the decision of the Board heretofore rendered in the above entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 6th day of April, 1933.

(Signed) C. M. Charest, General Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assign- [fol. 18] ments of errors mentioned therein, is hereby acknowledged this 8 day of April, 1933.

Rockford Life Insurance Company, (Sgd.) By Francis W. Brattle, Pres. Respondent on review.

BEFORE U. S. BOARD OF TAX APPEALS

NOTICE OF FILING PETITION FOR REVIEW—Filed April 19, 1933

To M. L. Seidman, C. P. A., 2 Lafayette Street, New York, New York:

You are hereby notified that the Commissioner of Internal Review did, on the 6th day of April, 1933, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Seventh Circuit, of the decision of the Board heretofore rendered in the above entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 6th day of April, 1933.

(Signed) C. M. Charest, General Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of errors mentioned therein, is hereby acknowledged this 11 day of April, 1933.

(Sgd.) M. L. Seidman, Attorney for Respondent on Review.

11d. 4/5/33.

[fol. 19] IN UNITED STATES CIRCUIT COURT OF APPEALS, SEVENTH CIRCUIT

PETITION FOR REVIEW—Filed April 6, 1933

To the Honorable Judges of the United States Circuit Court of Appeals for the Seventh Circuit:

Now comes David Burnet, Commissioner of Internal Revenue, by his attorneys, Sewall Key, Head of the Tax

Division of the Department of Justice, C. M. Charest, General Counsel, Bureau of Internal Revenue, and John D. Foley, Special Attorney, Bureau of Internal Revenue, and respectfully shows:

I

The petitioner is the duly authorized and acting Commissioner of Internal Revenue of the United States.

The respondent is a corporation organized and existing under the laws of the State of Illinois, with its principal office at Rockford, Illinois. Its income tax return for the calendar year 1929 was filed with the Collector of Internal Revenue for the 1st Collection District of Illinois, in the City of Chicago, State of Illinois, and within the territorial limits of the Seventh Judicial Circuit of the United States.

II

Prior to October 30, 1931, the petitioner determined that there was a deficiency in income tax of respondent for the calendar year 1929 in the sum of $607.53 and on said date petitioner advised respondent by registered mail of said deficiency. Respondent duly filed an appeal with the United States Board of Tax Appeals, hereinafter called the Board. The petitioner duly filed his answer to respondent's appeal and on September 28, 1932, the appeal was duly heard by the Board. On November 9, 1932, the Board entered its interlocutory decision wherein it found and adjudged that respondent was under no necessity to include in its gross income the rental value of space occupied by it in real estate owned by it as a condition to being allowed deductions for depreciation, taxes and expenses of the property so owned and occupied. The Board further held that respondent was entitled to deduct from its gross income the depreciation upon furniture and fixtures used in the underwriting [fol. 20] portion of its business as well as the depreciation of furniture and fixtures used in the investment portion of its business. Pursuant to the principles laid down in its interlocutory decision of November 9, 1932, the Board on January 24, 1933, entered its decision or order of redetermination wherein it redetermined and decided that there had been an overpayment of respondent's income taxes for the calendar year 1929 in the amount of $750.05.

III

The petitioner is aggrieved at the decision of the Board of Tax Appeals and says that in the proceedings before the Board and in the decision aforesaid, manifest error occurred and intervened to his prejudice and he assigns the following errors:

1. The Board erred in holding section 203(b) of the Revenue Act of 1928 unconstitutional.

2. The Board erred in failing to hold that the respondent was estopped to question the constitutionality of section 203(b) of the Revenue Act of 1928, by reason of having deducted taxes, expenses and allowances for depreciation in respect of its home office building when making its return for the calendar year 1929.

3. The Board erred in holding that the statutory requirement for the inclusion in gross income of the rental value of space occupied by respondent in its home office building was an attempt by Congress to treat such rental value as taxable income rather than as a mere limitation upon the amounts deductible on account of taxes, expenses and depreciation of said building.

4. The Board erred in failing to hold that section 203(b) of the Revenue Act of 1928 is sustainable as an excise tax laid upon the business of leasing property, collecting rents and managing an office building.

5. The Board erred in holding that respondent, a life insurance company, was entitled to deduct from its gross income depreciation sustained upon furniture and fixtures used in the underwriting portion of its business as well as the depreciation sustained upon furniture and fixtures used in the investment portion of its business.

Wherefore petitioner petitions that the decision of the Board be reviewed by the United States Circuit Court of Appeals for the Seventh Circuit, that a transcript of the [fol. 21] record be prepared in accordance with law and with the rules of said Court and transmitted to the clerk of said Court for filing, and that appropriate action be taken

to the end that the errors complained of may be reviewed and corrected by said Court.

(Sgd.) Sewall Key, Head, Tax Division. C. M. Charest, General Counsel, Bureau of Internal Revenue. Of Counsel: John D. Foley, Special Attorney, Bureau of Internal Revenue.

14d. 4/4/33.

Duly sworn to by C. M. Charest. Jurat omitted in printing.

[fol. 22] BEFORE U. S. BOARD OF TAX APPEALS

ORDER ENLARGING TIME—Entered June 6, 1933

For cause appearing of record, it is

Ordered: That the time for transmission and delivery of the record sur petition for review of the above entitled proceeding by the United States Circuit Court of Appeals, Seventh Circuit, be and it is hereby extended to July 15, 1933.

(Signed) Logan Morris, Member.

Dated Washington, D. C., June 6, 1933.

BEFORE U. S. BOARD OF TAX APPEALS

PRÆCIPE FOR RECORD—Filed May 25, 1933

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Seventh Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Seventh Circuit, heretofore filed by the Commissioner of Internal Revenue:

1. Docket entries of the proceedings before the Board.
2. Pleadings before the Board.

(a) Petition, including annexed copy of deficiency letter.
(b) Answer.

3. Opinion and decision of the Board, including stipulation of facts filed September 28, 1932, and agreement amending stipulation of facts filed October 7, 1932, which said stipulation of facts, as amended, has been adopted by the Board as its findings of fact.

4. Petition for review, together with proof of service of notice of filing petition for review and of service of a copy of petition for review.

5. Orders if any enlarging time for the transmission and delivery of the record.

6. This præcipe.

(Signed) C. M. Charest, General Counsel, Bureau of Internal Revenue.

[fols. 23-26] Service of a copy of the within præcipe is hereby admitted this 16 day of May, 1933.

(Sgd.) J: S. Seidman, Attorney for Respondent.

11d. 4/24/33.

Clerk's certificates to foregoing transcript omitted in printing.

[fols. 27 & 28] [Caption omitted]

Appearances of counsel omitted in printing.

[fol. 29] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

No. 5020

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

ROCKFORD LIFE INS. CO., Respondent

MOTION FOR SUBSTITUTION—Filed July 25, 1933

Comes now Guy T. Helvering, Commissioner of Internal Revenue, and moves the court that he be substituted for

David Burnet as petitioner herein, and in support of said motion respectfully shows:

1. That the resignation of said David Burnet, who was Commissioner of Internal Revenue when the petition for review in this proceeding was filed, was duly accepted and he ceased to be such officer on May 15, 1933.

2. That Guy T. Helvering was duly appointed and confirmed as Commissioner of Internal Revenue to succeed the said David Burnet; that he qualified as such officer and entered upon the duties of said office on June 6, 1933, since which date the said Guy T. Helvering has been and now is Commissioner of Internal Revenue.

3. That there is a substantial need for continuing and maintaining this proceeding and obtaining an adjudication of the questions involved, for otherwise the order of the United States Board of Tax Appeals herein sought to be reviewed will become final and the right to have the legality thereof determined will be extinguished.

This motion is made pursuant to the provisions of Section 11 of the Act of February 13, 1925, c. 229, 403 Stat. 941 (U. S. C., Title 28, Sec. 780).

Dated June 7, 1933.

Sewall Key, Special Assistant to the Attorney General, Attorney for Guy T. Helvering, Commissioner of Internal Revenue.

[fol. 30] The undersigned attorney for respondent herein hereby expressly consents to the substitution sought by the above motion.

J. H. Erdman, Attorney for Respondent.

[File endorsement omitted.]

IN UNITED STATES CIRCUIT COURT OF APPEALS

[Title omitted]

ORDER SUBSTITUTING PARTY PETITIONER—July 25, 1933

On motion of Guy T. Helvering, Commissioner of Internal Revenue, expressly consented to by the respondent, it

is hereby ordered that the said Guy T. Helvering as such officer, be, and he hereby is substituted for David Burnet, former Commissioner of Internal Revenue, and that this proceeding be so continued and maintained.

[fol. 31] Appearances of counsel omitted in printing.

[fol. 32] IN UNITED STATES CIRCUIT COURT OF APPEALS

[Title omitted]

ORDER SETTING CAUSE—Aug. 31, 1933

It is ordered by the Court that this cause be, and the same is hereby set down for hearing on October 12, 1933.

[fol. 33] Minute entry of submission, Oct. 12, 1933, omitted in printing.

[fol. 34] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT, OCTOBER TERM, 1933, OCTOBER SESSION, 1933

No. 5020

COMMISSIONER OF INTERNAL REVENUE, Petitioner,

vs.

ROCKFORD LIFE INSURANCE COMPANY, Respondent

Petition for Review of Decision of the United States Board of Tax Appeals

OPINION—Filed October 20, 1933

Before Alschuler, Evans, and FitzHenry, Circuit Judges

EVANS, Circuit Judge:

The two issues presented for determination by this appeal are identical with two presented in appeals Nos. 4993 and 4999, involving the Commissioner of Internal Revenue

and the Lafayette Life Insurance Company. The issues are: (1) The constitutionality of Section 203 (b) of the Revenue Act of 1928 requiring the reporting of rental value, calculated according to statute, of home office space occupied by taxpayer, if it seeks certain statutory deductions; (2) The deductibility of depreciation upon furniture and fixtures used in the underwriting department of the company.

The parties stipulated that the case be submitted on briefs without oral argument. In view of the similarity of issues in this cause and in appeals Nos. 4993 and 4999, Commissioner of Internal Revenue v. Lafayette Life Insurance Company, decided this day, the decision in these latter cases shall govern the disposition of this appeal.

It is therefore ordered that the order of the Board be, and it is hereby, reversed with directions to redetermine the tax of the respondent herein in accordance with the views expressed in the opinion in Nos. 4993 and 4999.

[fols. 35 & 36] IN UNITED STATES CIRCUIT COURT OF APPEALS

5020

COMMISSIONER OF INTERNAL REVENUE

vs.

ROCKFORD LIFE INSURANCE COMPANY

Petition for Review of Decision of the United States Board of Tax Appeals

JUDGMENT—Oct. 20, 1933

This cause came on to be heard on the transcript of the record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof: It is now here ordered and adjudged by this Court that the decision entered in this cause on January 24, 1933 by the United States Board of Tax Appeals be, and the same is hereby reversed; and that this cause be, and the same is hereby remanded to the said United States Board of Tax Appeals with directions to re-

determine the tax of the respondent herein in accordance with the views expressed in the opinion of this Court in Causes No. 4993, Commissioner of Internal Revenue vs. Lafayette Life Insurance Company, and No. 4999, Lafayette Life Insurance Company vs. Commissioner of Internal Revenue.

[fol. 37] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 38] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed February 5, 1934.

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Seventh Circuit is granted, and the case is assigned for argument immediately following No. 689, Helvering, Commissioner of Internal Revenue, vs. Independent Life Insurance Co.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 38,325. U. S. Circuit Court of Appeals, Seventh Circuit. Term No. 722. Rockford Life Insurance Company, Petitioner, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed January 17, 1934. File No. 722, O. T., 1933.

IN THE

Supreme Court of the United States

October Term, 1906.

ROCKFORD LIFE INSURANCE COMPANY, - Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR A WRIT OF CERTIORARI

TO THE

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

C. E. WELSH,
General Counsel,
WM. MARSHALL BULLITT,
Special Counsel.

LOUISVILLE LAW COMPANY, INCORPORATED, LOUISVILLE, KY.

[References required by Rules 12 and 27]

Opinion below. *Commissioner* v. *Rockford Life Ins. Co.*, 67 F. (2d) 213; R. _____

Jurisdictional authority. Judicial Code §240(a), as amended by Act of February 13, 1925.

Date of Judgment. October 20, 1933 (R. _____).

Nature of the case, rulings, etc. The taxpayer, a life insurance company, did not include in its gross income for 1929 any sum to represent the rental value of its home office building, owned and occupied by it; and it claimed as deductions (1) certain sums for depreciation, taxes and repairs on account of such property, and also (2) depreciation for certain furniture and fixtures.

The Commissioner determined a deficiency in income tax, which the Board of Tax Appeals rejected as contrary to its ruling in *Independent Life Ins. Co.*, 17 B. T. A. 757, and *Lafayette Life Ins. Co.*, 26 B. T. A. 947 (*Rockford Life Ins. Co.*, 27 B. T. A. _____, R. 17), and held that had been an overpayment (*Id.*).

The C. C. A. (7th) *reversed* the B. T. A., and held (1) that the Company must include as a part of its taxable income the rental value of space occupied by it in its own property, in order to entitle it to deductions for taxes, expenses, etc., and also (2) that depreciation for furniture and fixtures could only be allowed on the investment portion of its business (*Commissioner* v. *Rockford Life*, 67 F. (2d) 213).

IN THE

Supreme Court of the United States

October Term, 1933.

ROCKFORD LIFE INSURANCE COMPANY, - - - *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR A WRIT OF CERTIORARI

TO THE

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The Rockford Life Insurance Company petitions for a writ of *certiorari* to review a decision of the C. C. A. (7th Circuit), rendered October 20, 1933, in *Commissioner v. Rockford Life Ins. Co.*, 67 F. (2d) 213, which held:

(1) That §203(b) of the Revenue Act of 1928 (26 U. S. C. A., §2203(b)) was constitutional and

(2) That deductions for depreciation upon furniture and fixtures should be limited to the *investment portion* of the business only.

SHORT STATEMENT OF THE MATTER INVOLVED.

The Commissioner of Internal Revenue determined a deficiency in income tax for 1929, by disallowing (1) certain deductions claimed for depreciation, taxes and repairs on account of a Home Office Building, and (2) certain depreciation for furniture and fixtures (R. 5-8).

The Board of Tax Appeals *reversed* the Commissioner, and decided that the deductions were proper (*Rockford Life Ins. Co.*, 27 B. T. A. ——, R. 16).

The C. C. A. reversed the B. T. A., and sustained the Commissioner (*Commissioner* v. *Rockford Life Ins. Co.*, 67 F. (2d) 213, R. ——).

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT.

1. The decision of the C. C. A. (7th) below was in *direct conflict* with the decision of the C. C. A. (6th) [*Commissioner* v. *Independent Life Ins. Co.*, 67 F. (2d) 470] and of this Court in *National Life Ins. Co.* v. *U. S.*, 277 U. S. 508.

As conclusive evidence of the existence of such conflict between the C. C. A. of the 6th and 7th Circuits respectively, it is sufficient to point out that the Government has recently filed a petition for *certiorari* (now pending undetermined), in *Commissioner* v. *Independent Life Insurance Co.*, No. 689, October Term, 1933, wherein the reason assigned for the granting of the writ, is such conflict, in the following words (p. 5):

"The decision below is in direct conflict with the decisions of the Circuit Court of Appeals for the Seventh Circuit in *Commissioner* v. *Lafayette Life Insurance Co.*, 67 F. (2d) 209, and *Commissioner* v. *Rockford Life Insurance Co.*, 67 F. (2d) 213."

2. The Government points out additional reasons why a writ of *certiorari* should be granted in the *Independent Life* case [such as the holding by the C. C. A. (6th) that an important provision of the Federal Revenue Laws was unconstitutional, and its important connection with the system of taxing life insurance companies, affecting all life insurance companies which maintain offices in their own buildings, and the various claims for refund, etc.]

3. If, therefore, this Court shall deem it proper to grant a writ of *certiorari* to the Government in the *Independent Life Insurance Company* case, No. 689, October Term, 1933, then for exactly the same reason, it should also grant a writ of *certiorari* in the instant (*Rockford Life Insurance Company*) case, so that the holdings in both the 6th and 7th Circuits, which are in direct conflict, shall both be before this Court at the same time.

In view of the importance of the question, and this direct conflict between the C. C. A. of the 6th and 7th Circuits respectively—and both the Government and the Insurance Companies agree that such direct conflict exists—the *certiorari* should be granted in both the *Independent Life* case and in the *Rockford Life* case.

4. In the *Rockford Life* case, there is one additional question (not involved in the *Independent Life* case), which is not a question of constitutionality but of statutory inter-

pretation. This question, however, involves every life insurance company in the United States, and involves the question whether the allowable depreciation for furniture and fixtures applies to *all* the company's furniture and fixtures, or only such furniture and fixtures as are used in the *investment portion* of the business.

5. Two important constitutional questions are involved, to-wit:

First: Where a taxpayer owns and occupies its own real estate, is the reasonable value of the space so occupied, income which can be taxed by Congress as *income*, or is the taxation thereof really a *direct tax* levied upon the taxpayer's real estate, which cannot be levied without apportionment?

Second: Can Congress, in view of the decision in *National Life Insurance Co v. U. S.*, 277 U. S. 508, allow deductions for taxes, expenses and depreciation on real estate to taxpayers who *do not own* their own buildings, and yet require a taxpayer which *does own* his own building, to consent, in order to obtain the benefit of such deductions, to include within his taxable income the rental value of the space occupied by the taxpayer at his own building, which is in reality a tax on real estate, *i. e.*, a direct tax, without apportionment?

C. K. WELSH,
General Counsel,

WM. MARSHALL BULLITT,
Special Counsel.

12 January 1934.

In the Supreme Court of the United States

OCTOBER TERM, 1933

No. 722

ROCKFORD LIFE INSURANCE COMPANY, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT

The decision below is in direct conflict with the decision of the Circuit Court of Appeals for the Sixth Circuit in *Commissioner* v. *Independent Life Insurance Co.*, 67 F. (2d) 470, now pending before this Court on a petition for certiorari filed on behalf of the Commissioner of Internal Revenue, No. 689, current term. The question presented is an important one, involving the constitutionality of certain provisions of the Federal revenue laws. For

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these reasons, although we consider the decision below to be correct, we do not oppose the granting of the writ.

Respectfully submitted.

J. CRAWFORD BIGGS,
Solicitor General.

JANUARY 1934.

U. S. GOVERNMENT PRINTING OFFICE: 1934

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CITATIONS

Cases:

Atlantic Cleaners & Dyers v. *United States*, 286 U.S. 427 — 11

Commissioner v. *Independent Life Ins. Co.*, No. 689, current term — 4, 5, 6

Commissioner v. *Lafayette Life Ins. Co.*, 67 F. (2d) 209 — 9

Crooks v. *Harrelson*, 282 U.S. 55 — 11

Diamond Alkali Co. v. *Heiner*, 60 F. (2d) 505, reversed, 288 U.S. 502 — 10

Lewis v. *Commissioner*, 47 F. (2d) 32 — 11

Murphy Oil Co. v. *Burnet*, 287 U.S. 299 — 9

Northern Trust Co. v. *United States*, E.D.Mo., decided December 15, 1932 (333 C.C.H., p. 8145) — 11

Scott, Oreon E., v. *Commissioner*, C.C.A. 8th, decided February 16, 1934 (343 C.C.H., p. 9489) — 12

Statute:

Revenue Act of 1928, c. 852, 45 Stat. 791:

Sec. 23 — 10

Sec. 202 — 8, 14

Sec. 203 — 8, 10, 14

Sec. 204 — 10

Miscellaneous:

Treasury Regulations 74, Art. 976 — 16

H.Rep. No. 350, 67th Cong., 1st Sess., p. 14 — 9

S.Rep. No. 275, 67th Cong., 1st Sess., p. 20 — 9

In the Supreme Court of the United States

OCTOBER TERM, 1933.

No. 722

ROCKFORD LIFE INSURANCE COMPANY, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The memorandum opinion of the United States Board of Tax Appeals (R. 15) is not reported. The opinion of the Circuit Court of Appeals (R. 23) is reported in 67 F. (2d) 213.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered October 20, 1933 (R. 24). The petition for a writ of certiorari was filed January 17, 1934, and was granted February 5, 1934 (R. 25). The

jurisdiction of this Court rests upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether it is within the competency of Congress to deny deductions for real estate expenses and depreciation connected with the home office building of a life insurance company which owns the building and receives substantially no rent therefrom.

2. Whether a life insurance company which pays taxes only upon its investment income may deduct depreciation upon furniture and fixtures used in its underwriting department as well as those used in its investment department.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved will be found in the Appendix, *infra,* pp. 14–16.

STATEMENT

The facts, as stipulated by the parties (R. 13–15) and found by the Board of Tax Appeals (R. 15), are substantially as follows:

Petitioner is a life insurance company incorporated under the laws of Illinois. During 1929 petitioner owned and occupied a building which it acquired in 1926 at a total cost of $77,524.21. The book value as of December 31, 1929, was $71,176.23 (R. 13).

During 1929 petitioner occupied the entire building and received therefrom only $15 rent. In the same year the building suffered depreciation of $1,813.71 and the petitioner expended upon the building $1,808.03 as taxes and $411.31 as expenses for ordinary and necessary repairs. (R. 13.) These three items were deducted by petitioner in its return for the year 1929 (R. 15), but petitioner did not include in its gross income the rental value of the space occupied by it (R. 14). Petitioner also deducted the full amount of depreciation on furniture and fixtures used in its business.

The Commissioner of Internal Revenue disallowed the deductions claimed for taxes, expenses and depreciation on the building (R. 14, 15). He further held that depreciation on furniture and fixtures was allowable only with respect to such of those assets as were used in the investment department. In the absence of any specific allocation of the cost of such assets to the investment department, the Commissioner computed the allowance upon the basis of the ratio of investment income to total income, which resulted in an allowance of $292.56. (R. 7, 14.)

These adjustments resulted in the finding of a deficiency of $607.53 (R. 8). Petitioner appealed to the Board of Tax Appeals, which found that there was no deficiency and determined an overpayment of $750.05 (R. 16). The Circuit Court of Appeals reversed the decision of the Board (R. 24), and this Court granted certiorari (R. 25).

SUMMARY OF ARGUMENT

I

The first question has to do with the constitutionality of the provision of the revenue acts allowing life insurance companies to deduct from gross income the taxes, expenses and depreciation on real estate which they own and occupy, only upon condition that they include in gross income an amount representing the rental value of the space occupied by them. This question is discussed in the brief for the petitioner in *Commissioner* v. *Independent Life Ins. Co.*, No. 689, current term, to which the Court is respectfully referred.

II

The second question has to do with the allowance for depreciation of furniture and fixtures. The provision of the statute upon which petitioner relies authorizes a " reasonable " allowance for depreciation. This allowance is deductible from " gross income ", which includes only investment income. The Congressional policy to correlate deductions allowed life insurance companies to the limited income upon which they are taxed is clearly revealed by the statute and the committee reports. In view of this policy the court below held that an allowance for depreciation of furniture and fixtures used in the investment part of the business, without

any corresponding allowance in respect of furniture and fixtures used in the underwriting departments, constitutes a reasonable allowance within the meaning of the statute. We submit that any other allowance would be unreasonable. The decision is obviously in harmony with the purpose of Congress and is an accord with decisions which have been rendered in analogous situations.

ARGUMENT

I

The facts here differ slightly from those in *Commissioner* v. *Independent Life Ins. Co.*, No. 689, current term, although both cases involve the constitutionality of the provisions of the revenue laws relating to taxes, expenses, and depreciation on real estate owned and occupied by life insurance companies. Petitioner occupied the entire home office building, receiving only $15 by way of rent (R. 13). In its income-tax return for 1929 it claimed as deductions on account of the property sums aggregating $4,033.05, but did not include in gross income any amount representing the rental value of the space which it occupied (R. 13, 15). The Commissioner, instead of adding such rental value to its gross income, simply disallowed the deductions, presumably for the reason that they were less than the rental value which petitioner would

have had to report.[1] The result was more favorable to petitioner than if the Commissioner had allowed the deductions and added the rental value of the space occupied.

It is apparent, therefore, that petitioner is not in a position to contend that it has been subjected to a direct tax on its real estate. The only question open here is whether Congress could properly deny petitioner the privilege of deducting taxes, expenses, and depreciation on property which, for the most part, was productive of no taxable income. The purpose and practical effect of the statute are discussed at length in the brief for the petitioner in *Commissioner* v. *Independent Life Ins. Co.*, No. 689, current term. For the reasons there stated we submit that the limitation on the deductions, which in the case at bar results in the allowance of no deductions at all, is reasonable and within the competency of Congress.

The facts of this case furnish a striking illustration of the necessity for such a limitation. As has been stated, the building produced only $15 of taxable income. Yet the company seeks to deduct $4,033.05, by far the greater part of which must have related to the production of income which was

[1]

4 percent of book value	$2,847.05
Plus expenses, depreciation, taxes	4,033.05
	6,880.10
Minus rents from tenants	15.00
Rental value to be added	6,865.10

not taxable. Surely it cannot be said that the disallowance of the deductions in these circumstances is arbitrary or unreasonable. The $4,033.05 is analogous to the rent which the company would have to pay if it did not own its home office, and which would not be deductible under the statute. The statute, therefore, as applied here, makes for equality rather than inequality between a company which occupies its own building and one which does not. The inclusion of this amount in the computation of the tax liability would result in a tax upon something other than the net investment income which both Congress and the companies contemplated should be the subject of the tax.

II.

The Commissioner's action with respect to the allowance for depreciation of furniture and fixtures is not challenged upon any constitutional ground. The question presented is solely one of statutory construction.

The Commissioner prepared a depreciation schedule which showed that petitioner's furniture and fixtures had suffered depreciation in 1929 of $1,783.02 (R. 9). However, since the furniture and fixtures were used in the production of both investment income and underwriting income, he determined that a reasonable amount to be de-

ducted from investment income alone should be computed on the basis of the ratio of investment income to the total income. The total income was found to be $751,147.77, and the investment income $123,248.44. Using that ratio the Commissioner found that a reasonable deduction amounted to $292.56. (R. 7.)

Petitioner does not dispute the accuracy of the calculation but asserts a right to deduct the whole amount of depreciation, because of the absence of any limiting language in Section 203 (a) (7) (*infra,* p. 15). That section provides that the "gross income" may be reduced by "a reasonable allowance for the exhaustion, wear and tear of property, including a reasonable allowance for obsolescence." While there is no language in the subsection specifically limiting the allowance, there is limiting language in the definition of "gross income" which the deduction serves to reduce. Section 202 (a) limits gross income to that received from interest, dividends and rents, and Congress undoubtedly intended that the deductions should bear some relation to that limited income. The income from capital gains and the underwriting business is not taxed, and if the expense of earning this untaxed income were permitted to reduce the taxable income there would be the paradox of omitting certain income from the tax and reducing the remainder by the expenses of earning the omitted income.

The general policy with respect to the taxation of life insurance companies was revealed in the committee reports relative to the 1921 Act, where the following statement appears (67th Cong., 1st Sess., S.Rep. No. 275, p. 20; see also H.Rep. No. 350, p. 14):

> The proposed plan would tax life insurance companies on the basis of their investment income from interest, dividends, and rents, *with suitable deductions for expenses fairly chargeable against such investment income.* (Italics ours.)

The purpose of Congress to correlate deductions to the limited income taxed is further disclosed by other provisions of the statute. Section 203 (a) (5) limits the deductible business expenses to those concerned with the investment business, and Section 203 (b), as has been observed, imposes a condition upon the deductions for real estate expenses and depreciation, which is designed to prevent the deduction of expenses properly attributable to the production of income which is not taxed.

In view of this policy the court below held in *Commissioner* v. *Lafayette Life Ins. Co.*, 67 F. (2d) 209, that depreciation on furniture and fixtures used in the investment business alone constituted a reasonable allowance within the meaning of the statute. The case at bar was decided upon the authority of that decision (R. 24). It is evident that some weight must be given to the word "reasonable" in the statute. Cf. *Murphy Oil Co.* v. *Bur-*

net, 287 U.S. 299. To be "reasonable" the allowance must be, as the term implies, just, fair, and equitable. *Diamond Alkali Co.* v. *Heiner,* 60 F. (2d) 505, 510 (C.C.A. 3d), reversed on another issue, 288 U.S. 502. And we submit that it would be unreasonable to allow a deduction for the expenses of earning nontaxable income.

Nor is there any incongruity in computing the reasonable allowance under Section 203 (a) (7) in a different manner from the allowance under Section 23 (k) which is applicable to corporations generally. Section 203 (a) (7) does not refer to Section 23 (k), and the structure of the statute shows that Congress did not mean the same thing in both sections. Insurance companies other than life or mutual are taxable under Section 204. In the case of such companies gross income includes investment income, underwriting income, and capital gains. Section 204 (b) (1). Thus, the statute reaches all of the income of such companies and places them on a parity with corporations generally. It is, therefore, appropriate that they have similar deductions, and it is found that Section 204 (c) (9) permits the deduction of "a reasonable allowance for the exhaustion, wear and tear of property, as provided in section 23 (k)." We submit that the omission from Section 203 (a) (7) of a reference to Section 23 (k) is significant and lends support to our contention that Congress did not intend to allow life insurance companies to compute depre-

ciation on the same basis as corporations which were taxed on all of their income. This Court has recently pointed out that the same word may have different meanings when used more than once, even in the same section of a statute (*Atlantic Cleaners & Dyers* v. *United States,* 286 U.S. 427, 433), and we submit that there is a valid reason for making a distinction here, and that Congress undoubtedly had it in mind.

The result reached below is consistent with the decision in *Lewis* v. *Commissioner,* 47 F. (2d) 32 (C.C.A. 3d), where a taxpayer receiving both exempt and taxable income was limited in his deductions for expenses to those fairly attributable to the earning of taxable income. There was no statutory authority for limiting the allowance in that case, but the decision was based upon (p. 34) "the common sense meaning of the words of the statute" when read in connection with the evident policy of Congress.

The same principle was applied in *The Northern Trust Co.* v. *United States* (E.D.Mo.), decided December 15, 1932, not officially reported, but see 333 C.C.H., p. 8145, where it was held that since, under *Crooks* v. *Harrelson,* 282 U.S. 55, Missouri real estate could not be included in the gross estate for the purpose of computing the estate tax, neither could the executor's commission for handling such real estate be allowed as a deduction. A contrary result has recently been reached in *Oreon E. Scott*

v. *Commissioner* (C.C.A. 8th), decided February 16, 1934, not yet officially reported, but see 343 C.C.H., p. 9489, where it was held that commissions paid executors for selling Missouri real estate were deductible. However, the Circuit Court of Appeals' decision is based upon its conclusion (p. 9490) that the statute "'expressly leaves the meaning of 'administration expenses' to the State law" and that the State law compensates the executor "for all services rendered in the management and disposition of the *entire* estate." (Italics by the court.) Accordingly, that decision does not in any way weaken the principle for which we contend here. The effect of that decision is that the statute itself made the principle inapplicable in that case.

We submit that the statute here involved has been correctly construed to limit deductions from gross income to those items bearing a relation to the gross income. The record plainly shows that the investment income (gross income) comprised only one sixth of the total income (R. 7). Hence, it is logical to suppose that the depreciation of the furniture and fixtures was due largely to its use in the production of nontaxable income. The allowance of the full amount of the depreciation under these conditions would not be a " reasonable " deduction within the terms of the statute.

CONCLUSION

The decision below should be affirmed.

Respectfully submitted.

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APRIL 1934.

APPENDIX

Revenue Act of 1928, c. 852, 45 Stat. 791, 842:

SEC. 202. GROSS INCOME OF LIFE INSURANCE COMPANIES.

(a) In the case of a life insurance company the term "gross income" means the gross amount of income received during the taxable year from interest, dividends, and rents.

SEC. 203. NET INCOME OF LIFE INSURANCE COMPANIES.

(a) *General rule.*—In the case of a life insurance company the term "net income" means the gross income less—

* * * * * *

(5) *Investment expenses.* — Investment expenses paid during the taxable year: *Provided,* That if any general expenses are in part assigned to or included in the investment expenses, the total deduction under this paragraph shall not exceed one-fourth of 1 per centum of the book value of the mean of the invested assets held at the beginning and end of the taxable year;

(6) *Real estate expenses.* — Taxes and other expenses paid during the taxable year exclusively upon or with respect to the real estate owned by the company, not including taxes assessed against local benefits of a kind tending to increase the value of the property assessed, and not including any amount paid out for new buildings, or for

permanent improvements or betterments made to increase the value of any property. The deduction allowed by this paragraph shall be allowed in the case of taxes imposed upon a shareholder of a company upon his interest as shareholder, which are paid by the company without reimbursement from the shareholder, but in such cases no deduction shall be allowed the shareholder for the amount of such taxes;

(7) *Depreciation.* — A reasonable allowance for the exhaustion, wear and tear of property, including a reasonable allowance for obsolescence;

(8) *Interest.* — All interest paid or accrued within the taxable year on its indebtedness, except on indebtedness incurred or continued to purchase or carry obligations or securities (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from taxation under this title; and * * *.

* * * * *

(b) *Rental value of real estate.*—No deduction shall be made under subsection (a) (6) and (7) of this section on account of any real estate owned and occupied in whole or in part by a life insurance company unless there is included in the return of gross income the rental value of the space so occupied. Such rental value shall be not less than a sum which in addition to any rents received from other tenants shall provide a net income (after deducting taxes, depreciation, and all other expenses) at the rate of 4 per centum per annum of the book value at the end of the taxable year of the real estate so owned or occupied.

Treasury Regulations 74 (promulgated under the Revenue Act of 1928):

ART. 976. *Home office properties.*—No deduction shall be made for any taxes, expenses, or depreciation on account of any real estate owned and occupied in whole or in part by a life insurance company unless there is included in the return of gross income the rental value of the space so occupied. Such rental value shall not be less than a sum which in addition to any rents received from other tenants shall provide a net income (after deducting taxes, depreciation, and other expenses) at the rate of 4 per cent per annum of the book value at the end of the taxable year of the real estate so owned and occupied. For example, if the book value of a parcel of real estate owned and occupied in whole or in part by the company is $1,000,000, the rents received from other tenants $30,000, taxes and expenses $40,000, and depreciation $20,000, the company would have to include in its gross income a sum not less than $70,000 ($40,000 taxes and expenses, plus $20,000 depreciation, minus $30,000 rents from tenants, plus 4 per cent of $1,000,000) as the rental value of the space occupied by it in order to avail itself of the deductions of $40,000 and $20,000. In any case the rents received from other tenants must be included in gross income.

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SUPREME COURT OF THE UNITED STATES.

No. 722.—October Term, 1933.

Rockford Life Insurance Company, Petitioner, *vs.* Commissioner of Internal Revenue.	On Writ of Cetriorari to the United States Circuit Court of Appeals for the Seventh Circuit.

[May 21, 1934.]

Mr. Justice Butler delivered the opinion of the Court.

This case involves the validity of a deficiency assessment of 1929 income taxes made under the Revenue Act of 1928. Section 202 defines gross income to be that received from interest, dividends and rents. Section 203 (a) defines net income to be the gross less specified deductions including (5) "investment expenses," (6) "Taxes and other expenses paid during the taxable year exclusively upon or with respect to the real estate owned by the company . . . ." and (7) "A reasonable allowance for the exhaustion, wear and tear of property, including a reasonable allowance for obsolescence". Subsection (b) provides no deduction shall be made under (a) (6) and (7) "on account of any real estate owned and occupied in whole or in part by a life insurance company unless there is included in the return of gross income the rental value of the space so occupied. Such rental value shall be not less than a sum which in addition to any rents received from other tenants shall provide a net income (after deducting taxes, depreciation, and all other expenses) at the rate of 4 per centum per annum of the book value at the end of the taxable year of the real estate so owned or occupied". 45 Stat. 842-844.

During 1929 petitioner owned a building all of which it used. It received $15 rent for use of the premises and in its return included that amount as a part of gross income. It did not add any sum on account of rental value of the building. Nevertheless, it deducted expenses chargeable to the building, amounting to $4,033.05. The commissioner disallowed the deduction. Petitioner also deducted from gross $1,783.02 to cover depreciation on all

furniture and fixtures. The commissioner held the deduction allowable only in respect of such as were used in connection with the company's "investment business". That phrase may be taken to include activities relating to interest, dividends and rents constituting the income taxed as distinguished from its "underwriting business" which embraces its other activities. There being no allocation, the commissioner apportioned depreciation on the ratio of investment income, $123,248.44, to total income, $751,147.77. This reduced the deduction to $292.56. These adjustments resulted in a finding of deficiency of $607.53. Following its earlier decisions, the Board of Tax Appeals held petitioner entitled to deduct expenses chargeable to the building and depreciation of all its furniture and fixtures. On that basis it found an overpayment of $750.05. The Circuit Court of Appeals reversed. 67 F. (2d) 213.

The ruling of the lower court disallowing deduction of expenses chargeable to the building is sustained on the authority of *Helvering* v. *Independent Life Ins. Co.*, decided this day.

The other question presented for decision is whether petitioner is entitled to deduct depreciation on all furniture and fixtures or only such part as fairly may be attributed to the income taxed. Petitioner raises no question as to the method employed for making the apportionment, but insists that the "reasonable allowance" granted by § 203 (a) (7) extends to all property and includes depreciation of all furniture and fixtures. It refers to the language of the corresponding provision in the Revenue Act of 1916 which permits deduction of "a reasonable allowance for the exhaustion, wear and tear of property *arising out of its use or employment in the business or trade*" and to similar language in the Revenue Act of 1918.[1] It emphasizes absence from the Act of 1921 and later ones of the words above italicized. It argues that the change of language, made applicable to life insurance companies, shows that Congress intended to permit them to deduct depreciation of all property without regard to its use. The constructions put upon provisions in measures that did not limit income to be taxed, as did later Acts, are of no value as guides to the meaning of the clause under consideration. In reason the cost of depreciation, like other items of expense to be deducted, ought to be limited to that related

[1] The Revenue Act of 1916, § 12 (a), 39 Stat. 768. 1917, § 4, 40 Stat. 302. Revenue Act of 1918, § 234 (a) (7), 40 Stat. 1078.

to the income taxed. Allowance of deduction of expenses incurred for the collection of premiums or in respect of other income not taxed would be hard to justify. In absence of specific declaration of that purpose, Congress may not reasonably be held to have intended by that means further to reduce taxable income of life insurance companies.

There is adequate evidence that Congress intended to limit deductions of expenses to those related to the taxed income. *Helvering* v. *Independent Life Insurance Co., supra.* In the reports of committees having in charge the Act of 1921 in which first appeared the language under consideration, § 203 (a) (7), it is said: "The proposed plan would tax life insurance companies on the basis of their investment income from interest, dividends, and rents, with suitable deductions for expenses fairly chargeable against such investment income".[2] Section 203 (a) (5), by restricting deductions to investment expenses, indicates purpose to exclude those not related to investment income. Section 203 (b), by condition imposed, similarly restricts deductions of real estate expenses. The language under consideration opposes deduction of unrelated expenses and is in harmony with the construction for which the commissioner contends. The significance of the word "reasonable" qualifying allowance need not be limited to the amount to be ascertained. But having regard to the context and probable purpose of the provision it rightly may be construed to limit the ascertainment of depreciation to the property that is used in connection with the company's investment business. The construction put upon the statute by the Commissioner and Circuit Court of Appeals is sustained.

Affirmed.

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[2] 67th Congress, 1st Session, Senate Report No. 275, p. 20. See also House Report No. 350, p. 14.

A true copy.

Test:

Clerk, Supreme Court, U. S.